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IN THE

Supreme Court of the United States

OCTOBER TERM 1961

No. 363.

THE O LIQUIDATING CORPORATION,
Petitioner,

against

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

PETITIONER'S REPLY BRIEF.

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Preliminary Statement.

The Respondent is incorrect in stating at page 5 of his brief that the decision of the Tax Court would have relieved the taxpayer "entirely of its income and excess profit tax liability for this item for the year 1952". The dividend received in 1952 had been included in 1951 and had borne its full tax. The dividend received in 1953 would, under the Tax Court decision, be included in 1953 and subjected to its full tax. The dividend received in 1954 was included for tax purposes in 1954 and properly subjected to the 1954 rates. In fact every dividend down through the years will have been included for tax purposes in some year.

I.

Beacon Publishing Co. v. *Commissioner* (C. A. 10), 218 F. 2d 697 cannot be distinguished factually.

"• • • for years prior to 1943 and 1944 Beacon carried these accounts (prepaid subscriptions) on its books as cash items • • •" (218 F. 2d 701). Thus the prepaid cash subscriptions received in 1940 and 1941 had been included in the income reported in those years, respectively. However, under the principle applied in *Beacon*, this did not prevent Beacon from correcting the error in later years.

The question was squarely presented in *Beacon*. The Commissioner argued in his *Beacon* brief, page 16:

> "Further, taxpayer could not effect a change in its method of accounting without the prior approval of the Commissioner, which here was neither applied for nor granted."

In answer to this the Tenth Circuit stated (p. 702) that "• • • we have no doubt but that a taxpayer may, without the consent of the Commissioner, apply the method of accounting which he has adopted, though not theretofore applied to a particular item, when that change will correct errors and clearly reflect income."

The correction made by the petitioner in the case at bar did not have the effect of placing either the 1953 dividend or the 1954 dividend beyond the reach of the tax collector. The taxes "due" on these items have been paid. The limitation mentioned by the Tenth Circuit does not apply since the correction did not result "• • • in the avoidance of the payment of taxes due."

Even if, in spite of the Statute of Limitations (see *Rothensies* v. *Electric Storage Battery Co.*, 329 U. S. 296,

301), consideration could now be given to what happened in the years since 1918 or 1941 the Commissioner's position would not be improved. The record here does not show whether, by reason of the prior errors, the taxpayer paid more or less taxes than would have been paid had the item been properly handled. Tax rates varied. There were increases and reductions. The taxpayer's income necessarily varied. Certainly every dividend bore a tax. None escaped. If relevant at all, the burden in this respect rested upon the Commissioner (see Frankfurter, C. J. in *Ross* v. *Commissioner* (C. A. 1), 169 F. 2d 483 at page 496).

Circuit Judge, L. Hand has pointed out the futility of trying to go back through the years to determine where equities may rest (*Bennet* v. *Helvering* (C. C. A. 2), 137 F. 2d 537 at page 538).

The Supreme Court has recognized that the basic distinction made in *Beacon* was the correction of an error *versus* a change in accounting. Thus in *Automobile Club* v. *Commissioner*, 353 U. S. 180, Mr. Justice Brennan said at page 189 note 20:

> "In *Beacon*, performance of the subscription, in most instances, was, in part, necessarily deferred until the publication dates after the tax year."

Since the prepaid subscriptions were "necessarily deferred until the publication date after the tax year" the prior way of handling those items was erroneous and could be corrected.

Beacon is regarded in the Second Circuit, at least, as authority for the proposition that the correction of an error is not a change in accounting method (*Bressner Radio Inc.* v. *Commissioner* (C. A. 2), 267 F. 2d 520, 523).

A quagmire, in an already complex subject, will inevitably result unless the principle is strictly observed that the taxpayer's return must "clearly reflect income."

This was reaffirmed, quite recently, by Mr. Justice Whittaker, writing in *United States* v. *Consolidated Edison*, 366 U. S. 380 at page 385:

> "And the parties agree that, under the applicable federal statutes, neither the Government nor an accrual-basis taxpayer may cause an item to be deducted in a year other than the one in which it accrued."

Conclusion.

The petition for a writ of certiorari should be granted.

Respectfully submitted,

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Counsel for Petitioner.

October 2, 1961.